

Budget Issues Summary

Legislators of the First Regular Session of the Fifty-seventh Idaho Legislature faced one of the most challenging fiscal situations since the beginning of the modern era over 30 years ago when the Legislature began meeting in annual sessions. A dismal national economic picture continued to drive Idaho revenue collections below expectations, forcing the Governor and the Legislature to come to grips with a budget shortfall approaching 10%. The Governor's spending plan called for a cent and a half increase in the sales tax and an increase in the cigarette tax.

After a record-setting 118-day session, the Idaho Legislature ultimately settled on a budget blueprint that called for a one-cent sales tax increase, a cigarette tax increase, and a spending plan that cut about \$20 million from the Governor's budget recommendation. While resolving the revenue and spending issues was a lengthy and difficult process, Idaho is one of the few states in the country to have closed its budget gap and brought ongoing spending commitments in line with ongoing revenues.

Fiscal Year 2003 Budget Issues

The Economic Outlook Committee projected that ongoing revenues would increase 3.7% over the previous year, yielding about \$1.753 billion for the FY 2003 budget. However, the original ongoing spending commitments for the current year were about \$1.967 billion, a difference of \$214 million. The Legislature closed the majority of that gap by transferring all of the state's available cash reserves, which totaled about \$192.8 million, to the General Fund. The remainder of the gap was closed with a one-cent sales tax increase that went into effect May 1, generating about \$13 million for the current year, and by a spending reduction plan that reduced most state agency budgets 3.5% (public schools and higher education were exempt) and saved about \$19.5 million. It remains to be seen if revenues will ultimately attain projected levels for the year.

Fiscal Year 2004 Budget Issues

The fiscal year 2004 budget was based upon a revenue projection of 4.3% over the FY 2003 ongoing projection. The biggest challenge for FY 2004 was replacing the \$192.8 million in one-time money used to support FY 2003. Ultimately the Legislature enacted a combination of selected budget reductions and tax increases. The average budget reduction for most small- to medium-sized agencies was 5.7%. Those agencies and institutions that received increases were public schools (2.5%), higher education (2.1%), and Health and Welfare (4.5%). Overall, General Fund spending increased 1.8% from the original FY 2003 appropriation (see the table on page 22). However, in order to support this budget, primarily to protect Education and Health and Welfare, the Legislature also increased revenues about \$183 million, enacting a one-cent sales tax increase expected to generate about \$160 million and increasing the cigarette tax from 28 cents to 57 cents per pack.

For the second year in a row there was no funded salary increase for state employees, although about two-thirds of the anticipated increase in health insurance costs was covered with an appropriation.

JFAC Down-time & Splitting the Committee

The difficult and challenging fiscal conditions created some unique circumstances for the Joint Finance Appropriations Committee. The budget hearing process finished up in typical fashion on Wednesday, February 19th after about five and a half weeks of reviewing agency budget requests. However, at that point in time there were no additional revenue bills introduced to cover any portion of the budget gap, so JFAC began setting budgets for several small and medium sized agencies based on no new revenues, which would require budget reductions of about 7.1%. This initial round of budget-setting took place from February 24th through March 4th after which there were still no revenue bills and the remaining budgets to set included Education, Health and Welfare and Corrections, so JFAC adjourned until House and Senate leadership and the Governor could agree on a big picture solution. When these negotiations seemed deadlocked, the House majority leadership convened the House appropriations committee by itself and passed all the remaining twenty-nine appropriations over a two day period April 23rd and 24th. However, the Senate Finance Committee never heard those bills. Ultimately JFAC reconvened after a sales tax bill passed and after a conference committee hammered out a compromise on a cigarette tax proposal. JFAC finished the remaining budgets between April 29th and May 2nd.

Public Schools: The General Fund appropriation for public schools increased by 2.5% in FY 2004, from \$920 million to \$943 million. A detailed comparison of the public schools program distributions for FY 2003 and FY 2004 is charted after the Public Schools program summary. Previously set in one bill, the public schools appropriation was set using a new, five-division format for FY 2004 — Administrators, Teachers, Operations, Children's Programs and Facilities. The budget also reflects, for the first time, the federal funds passed through by the state to local school districts. These pass-through funds had previously been included in the budget of the Superintendent of Public Instruction, which still includes the federal funds that pay for the personnel and operating costs of administering these grants. The budgets for the five divisions, along with attached statutory changes, are summarized as follows:

Division of Administrators (SB 1197)

The budget for the Division of Administrators includes increased funding for estimated enrollment growth equal to 125 new classroom units. It includes normal annual adjustments in the estimated costs of the Early Retirement Program, and funding for the administrators' portion of Achievement Standards Implementation, which is funded 25% from the General Fund and 75% from federal funds. The appropriation also includes three statutory changes. The first caps the experience and education index for administrators. This change is not likely to have any significant effect, since the index for administrators varies little from year to year. It is, however, consistent with the approach for the Division of Teachers. The second change removes the "use it or lose it" provision for administrative staff funding. This will not cost or save the state any money but will provide greater flexibility to local school districts. If districts are able to save money in the area of administrative staffing, they will no longer be required to return the savings to the state, but could instead retain the money as discretionary funds to be spent on local priorities. The third change phases out administrator participation in the early retirement program. The program is still funded in the FY 2004 budget to provide payouts for administrators who are currently applying for early retirement. Administrator participation would end, however, on September 1, 2003, preventing administrators from applying in the future for early retirement.

Division of Teachers (HB 456)

The budget for the Division of Teachers includes increased funding for estimated enrollment growth equal to 125 new classroom units. It also includes normal annual adjustments in the estimated costs of the Early Retirement Program, the Teacher Incentive Award, and funding for the teachers' portion of Achievement Standards Implementation, which is funded 25% from the General Fund and 75% from federal funds. The appropriation includes one statutory change, a cap on the experience and education index for teachers. This change is unlikely to affect hiring decisions, since the cap is allocated proportionately. In the future, the Legislature will annually review the issue of providing state funding for teacher pay increases, rather than have such increases automatically funded through increases in the index. The effect of this change will be to have the issue of increasing funds for teacher pay treated more like a change in employee compensation (CEC) decision for state employees.

Division of Operations (HB 463 & HB 467)

The budget for the Division of Operations increases funding for estimated enrollment growth equal to 125 new classroom units. It includes normal annual adjustments in the estimated costs of Transportation, Property Tax Replacement, and funding for centrally offered Achievement Standards Implementation training opportunities, which is funded 25% from the General Fund and 75% from federal funds. This budget also funds technology at the current FY 2003 level, provides sufficient discretionary funds to maintain total discretionary funding at the same

\$24,447 per classroom unit level that was estimated for the current FY 2003 budget, and places \$7.1 million in the new Public Education Stabilization Fund.

The Operations budget includes three areas of statutory changes. The first deals with the creation and workings of the Public Education Stabilization Fund. The fund could be used to: 1) offset the public schools' proportional share of any midyear General Fund budget cut; 2) replace funds lost to public schools through a reduction in endowment distributions; 3) distribute to public schools any funds necessary to maintain per-support-unit discretionary funds at the level promised by the state, such as would be necessary if the state underestimated enrollment growth; and 4) loan to school districts negatively impacted by the future 110% cap on transportation costs, in cases where the school district is unable to create greater efficiencies, unable to secure an exemption from the State Board of Education, and unable to absorb the impact through the use of fund balances. Borrowed

moneys would be paid back from the school district's transportation reimbursement in the following year. Given the lack of rebound in the investment markets and endowment losses, public schools face a potential \$8.5 million shortfall in FY 2003 and a \$6.2 million shortfall in FY 2004. Because there is no stabilization fund in FY 2003, public schools will be forced to absorb the shortfall in the current year. For FY 2004, however, there is \$7.1 million in the Public Education Stabilization Fund that can be used to offset the projected \$6.2 million FY 2004 shortfall and maintain discretionary funding at the \$24,447 per classroom level.

The second area of statutory change deals with the setting of a \$75 million cap on Property Tax Replacement funding. Since \$73 million is required for FY 2004, this cap will not affect the FY 2004 budget. It will almost certainly, however, affect the FY 2005 budget, since local assessed property values have been increasing by an average of about 6% for the last several years. This change will not cause any automatic shift to or increases in local property taxes. School district maintenance and operations levies are still limited to the same three-tenths of 1% that exist currently. School districts would not, however, continue to receive revenue growth based on increases in assessed property values for the one-tenth of 1% that the state has funded since FY 1996.

The third area of statutory change deals with changes to the transportation program. Under the first of these changes, the state would only reimburse for the "basic bus," plus safety features and handicap accessibility features. Additional features would be paid for by the school district. Reimbursable expenses would be capped at 110% of the statewide average in FY 2005. This cap would reduce to 105% in FY 2006 and 103% thereafter. Districts would be able to use the better of their cost per mile or cost per student, as compared to statewide averages for those measures, since urban districts tend to have more efficient costs per student, while rural districts do better with cost per mile.

Division of Children's Programs (SB 1198)

The Division of Children's Programs includes programs providing direct educational or material benefits to children, where funding does not primarily go to paying certificated teachers and administrators. It also includes programs that primarily and specifically provide funding for the separate instruction of identified subgroups of children outside the normal classroom of an Idaho public school. Appropriation highlights include the first state appropriation, in the amount of \$450,000, for the costs of the Idaho Digital Learning Academy (IDLA). This provides funding for the cost of providing online course materials, often for students in small, rural school districts with limited course offerings. The IDLA, through separate legislation, has been given the authority to charge fees to school districts whose students utilize IDLA services. This, too, will help offset the cost of the program. When this system is fully implemented, it is estimated that the need for state support will decline to \$300,000 a year.

The appropriation for the Division of Children's Programs also provides blanket authority to the State Department of Education to transfer funds between the five divisions of the public schools budget, in any amount necessary, in order to comply with appropriations and Idaho's public schools funding statutes.

Division of Facilities (SB 1196)

The Division of Facilities budget appropriates the State Lottery distribution to public schools "on budget," for the first time. It also utilizes \$825,000 of these lottery funds, which are for public school buildings, for the state's Bond Levy Equalization program (SB 1474, 2002), which provides a state subsidy for public school building construction. The Bond Levy Equalization law and fiscal note attached to SB 1474 did not specify from which source funds would be made available for this program.

College and Universities: The FY 2004 appropriation for the general education programs at the state's four-year college and universities (Boise State University, Idaho State University, University of Idaho, Lewis Clark State College) reflects a 2.1% General Fund increase and a 35% dedicated fund increase. The increase is 11.1% for all funds. This appropriation receives no federal funds. The large dedicated fund increase is due to two years of student fee increases being included in the FY 2004 appropriation. In a typical year, the Legislature sets the higher education appropriation prior to the State Board of Education's April meeting, at which time the Board determines the student fee increase for the coming fiscal year. This year, the College and Universities appropriation had not been set by April 17 when the Board approved up to a 10% student fee increase. Since the \$14.9 million of new FY 2004 fee revenue was known when the Joint Finance-Appropriations Committee set the appropriation on May 2, it was included in the appropriation along with the FY 2003 fees of \$15.2 million that were generated by a 12% fee increase last year. As a result, for the first time, two years of student fee increases are included in a single-year appropriation.

Higher education received funding for several maintenance of current operations (MCO) items for FY 2004: a total of \$3,315,400 was included to cover increases in the employer-paid benefit costs as recommended by the Governor; \$473,900 will pay for interagency State Treasurer, Controller and insurance billings; \$651,900, or just under 50% of the requested amount, will pay for the state's portion of enrollment growth known as Enrollment Workload Adjustment; a fund shift totaling \$1,085,800 moves dedicated fund increases to the General Fund. This is the amount of MCO increases that would normally be carried by student fees and endowment funds. On a final note, due to poor investment performance, the earnings from the dedicated endowment funds decreased by \$1,701,700 but were not replaced with General Fund money, which was a consistent approach for all institutions impacted by endowment fund performance.

The change in General Fund money contained in the FY 2004 appropriation for the Community Colleges (North Idaho College and College of Southern Idaho), the Division of Professional-Technical Education and the Agricultural Research and Cooperative Extension Service matched the 2.1% increase provided in the College and Universities appropriation.

Department of Health and Welfare: Funding for the Department of Health and Welfare totaled \$374.9 million, which is approximately 18.8% of General Fund expenditures passed by the Idaho Legislature for FY 2004. This level of funding represents an increase of \$15.2 million, or 4.2%, over the department's FY 2003 original appropriation. At the same time, the number of authorized positions for the department was reduced by about 194 full-time positions.

This budget received a base reduction of 2%, or \$7.7 million, that impacted programs within Health and Welfare in a variety of ways. It also included: \$2.6 million to cover personnel cost rollups; \$25.3 million to cover a 3% medical inflationary increase in Medicaid and the state hospitals; \$36.8 million to cover caseload increases in Medicaid, increases in insurance costs, and adjustments in Attorney General, State Controller, and State Treasurer fees; and \$200,000 to annualize an approved supplemental appropriation to cover certain costs associated with the involuntary detention of persons with mental illness. In addition, \$3.2 million was shifted from federal funds to the General Fund to cover changes in the federal match rate, and \$120,000 was shifted from the Alcohol Intoxication Treatment Account to the General Fund for continued support of substance abuse services. A fund shift of \$415,600 from endowment funds to the General Fund was not authorized, remaining consistent with the manner in which the Legislature treated such fund-shift requests in other programs. Other policy adjustments that were made are as follows:

- Family and Community Services – \$177,200 was added to provide a 4% increase in foster care payments for those children who are hard to place, and \$443,400 was added to partially restore reductions made earlier in Sheltered Workshops.
- Indirect Support Services – Twelve administrative staff were reduced for a savings of \$940,700, and 100 unfunded vacant positions were eliminated.
- Medicaid – \$657,800 was added for Residential Rehabilitation, \$327,900 for Targeted Service Coordination, and \$499,900 for Targeted Case Management to partially restore previous reductions in these areas. In addition, \$750,000 was added to enhance dental services for adults by providing limited preventive and restorative services to all Medicaid adult clients.
- Division of Public Health Services – \$600,000 for the purchase of Prevnar Vaccine was shifted from the state to insurance companies for those children having health insurance. This vaccine reduces the chance of children getting pneumococcal infections that can cause such things as ear infections and meningitis and result in long-term complications or death. Currently, the federal Vaccine for Children funding pays the cost of vaccine for children covered by Medicaid and for Native American children. The state has paid for vaccine for all other children, both those uninsured and those insured.
- Division of Welfare – Eligibility determination for Medicaid and Food Stamps was shifted to the federal government for those individuals qualifying under the Supplemental Security Income program, for a savings of \$500,000 and a reduction of 4.5 positions.

Department of Correction: The FY 2004 appropriation for the Department of Correction totaled \$125,240,400, or 2.8% less than the FY 2003 original appropriation. The department received \$109 million in General Funds for FY 2004, or 2.9% less than its FY 2003 original appropriation. Because the Legislature followed the Governor's

recommendation and permanently removed \$2.3 million from county payments in FY 2003 (above the 3.5% budget reduction), and transferred the bond payment for the Idaho Correctional Center to the Department of Administration budget, the actual difference between the FY 2003 total appropriation and the FY 2004 original appropriation from the General Fund is \$7,058,000, a 6.9% increase. Using the same approach and comparing all funds, the increase over FY 2003 is \$5,824,700, or 4.9%.

- Inmate Growth – The forecast for prison growth for FY 2003 was 350, and by the middle of May remains relatively flat at nine. At the beginning of the legislative session the growth for FY 2004 was forecast at 488.
- Base Reductions – The only base reduction experienced in this agency was \$106,000 in the Support Services Division. All prison facilities, including Offender Programs and Community Supervision, were held harmless from further base reductions.
- Replacement Items – Significant difference between the bottom line approved by the Legislature and the Governor's recommendation reflects a reduction of \$1,001,000 for replacement items. The department received \$783,300 for replacement items.
- Contracts – In order to maintain the contract and accommodate projected growth in offenders, the funding for medical services was increased by \$1.2 million, a 10.7% increase from FY 2003. Funding to operate the Idaho Correctional Center was increased by \$985,300, or 4.8%, to meet contractual obligations and to insure the facility.
- Community Supervision – Ada County notified the state last year it would not continue to pay for pre-sentence reports for felony offenders. In accordance with Idaho Code the state picked up this responsibility at a cost of \$719,500 and 10.5 new employees. Funding of \$371,700 in General Funds for six new staff was authorized by the Legislature to handle the growth in probation and parole caseloads; \$1,110,900 was added for six new probation and parole officers and for one support staff to implement a legislative initiative to restore funding for transitional services and substance abuse treatment services in the community for 400 offenders, including parolees and probationers. Included in this funding was \$25,000 for community transitional services for a pilot Reentry Drug Court for 25 offenders. The Commission of Pardons and Parole received double the staff and funding recommended by the Governor in enhancements to expediently process parole violations and to expand the hearing officer program to another area of the state.
- Other – Adding modular units, expanding the East Boise Community Work Center and sheltering offenders in tents at St. Anthony added \$262,300 to FY 2004 operation costs.
- Contingency Fund – \$1 million from the General Fund was appropriated to the Department of Correction, to be made available only upon a request by the Board of Correction to the Governor if additional funds are necessary to support the prison population.

Permanent Building Fund Projects: For FY 2004, the Permanent Building Fund will be used primarily to address building maintenance projects. During FY 2003, \$35 million in Permanent Building Fund maintenance projects were canceled and the money was transferred to the General Fund as part of the effort to balance the state's General Fund budget. To partially address those cancellations, SB 1189 approved \$26.3 million in Permanent Building Fund moneys for maintenance ("alteration and repair") projects. These projects will be completed in order of priority as determined by the Division of Public Works, in coordination with state agencies.

The FY 2004 Permanent Building Fund appropriation also authorized two additional capital projects.

- The first project is for \$2 million, which reflects the Legislature's second authorization of funding for new electronic locking systems for the Idaho Maximum Security Institution (IMSI) and the Idaho Correctional Institution at Orofino. The Legislature approved about \$3 million for this project in FY 2003, but the Governor placed \$2 million of the project on hold as a budget balancing measure. Following the Governor's administrative decision to withhold two-thirds of project funding, the Joint Finance-Appropriations Committee in October 2002 reaffirmed its earlier decision that the project should go forward with the full \$3 million in funding. However, the Governor maintained the administrative holdback of the \$2 million for the project. In SB 1189, the Legislature has once again approved the balance of the funding for the electronic locking systems.

- The second project reflects \$700,000 for the third and final phase of the statewide microwave communication system. The system will provide improved communication for the state's public safety agencies and will allow Idaho Public Television to convert from analog to digital transmission.

A more detailed description of Permanent Building Fund expenditures and revenues can be found in the General Government section of this publication.

Facilities Bonding: Two related legislative measures provide for the bonding for eight new facilities across the state. Seven of these facilities are associated with higher education institutions, while one facility will be built for the Idaho State Police. Seven of the eight facilities had been at least partially funded previously with Permanent Building Fund moneys, but were canceled as part of the General Fund budget-balancing efforts for FY 2002 and FY 2003. House Concurrent Resolution 30 authorizes various state institutions, community college districts and the Department of Administration to enter into agreements with the Idaho State Building Authority to provide for the sale of bonds to finance the construction of the facilities.

The following table lists the facilities authorized in HCR 30:

<i>INSTITUTION/AGENCY</i>	<i>FACILITY</i>	<i>LOCATION</i>	<i>AMOUNT</i>	<i>CUM. TOTAL</i>
N. Idaho College	Allied Health	Coeur d'Alene	\$ 10,994,000	\$ 10,994,000
Univ. of Idaho	Teaching Ctr.	Moscow	\$ 11,729,000	\$ 22,723,000
Lewis-Clark St. College	Activity Ctr.	Lewiston	\$ 10,868,000	\$ 33,591,000
BSU	W. Campus	Nampa	\$ 8,655,000	\$ 42,246,000
Idaho State Police	Training Ctr.	Meridian	\$ 2,286,000	\$ 44,532,000
ISU	Multi-use Ctr.	Pocatello	\$ 12,177,000	\$ 56,709,000
E. Idaho Tech. College	Health Ed.	Idaho Falls	\$ 6,360,000	\$ 63,069,000
College of S. Idaho	Fine Arts Ctr.	Twin Falls	\$ 5,402,000	\$ 68,471,000

The annual debt payment on the bonds will begin in FY 2005 and is estimated to be between \$5.25 and \$5.75 million per year over a 20-year period. Bond payments will be made from the Permanent Building Fund. A related measure, HB 396, specifically authorized community college districts to enter into agreements with the State Building Authority. In short, HB 396 allows community college facilities to be financed with bonds issued by the State Building Authority. Also, the Legislature passed HB 397 that restricted the use of the Permanent Building Fund as a source for paying off bonded indebtedness beyond that authorized by the Legislature prior to June 30, 2003. The Governor, however, vetoed HB 397.

Idaho Millennium Fund: Due to revenue shortfalls in FY 2003, the Legislature transferred to the General Fund \$16.3 million from the April tobacco settlement payment, as well as the balance of the Millennium Fund, approximately \$40.3 million. In the 2002 legislative session, \$10 million from the 2003 tobacco payments was obligated and transferred to the General Fund for FY 2003. As a result, the entire amount of tobacco settlement payments received in 2003 went to the General Fund.

Budget Stabilization Fund: Last session the Legislature authorized the transfer of \$26,700,000 (SB 1517) from the Budget Stabilization Fund to the General Fund to balance the FY 2003 budget. This session, as the shortfall worsened, SB 1195 transferred the remaining \$26,390,000 balance from the Budget Stabilization Fund to the General Fund. The two transfers eliminated \$53,090,000, the equivalent of 2.7% of the final 2003 appropriation, leaving a balance of just \$34 in the Budget Stabilization Fund.